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In the Supreme Court of the United States

OCTOBER TERM, 1937

No. 55

MARY DUKE BIDDLE, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT

OPINIONS BELOW

The opinion of the United States Board of Tax Appeals (R. 103–119) is reported at 33 B. T. A. 127. The opinion of the Circuit Court of Appeals (R. 580–585) is reported at 86 F. (2d) 718.

JURISDICTION

The judgment of the Circuit Court of Appeals for the Second Circuit was entered December 14, 1936 (R. 586). This Court granted an extension of 60 days in which to file a petition for cer-

tiorari. Petition for certiorari was filed May 12, 1937, and was granted October 11, 1937. (R. 587.) The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION PRESENTED

The taxpayer received dividends upon capital stock in certain British corporations. Such dividends were declared and paid either "less tax" or "free of tax." The dividend warrants were accompanied in each instance by certificates, required by British law, certifying that all British and United Kingdom income taxes due on the profits of the company of which the dividends formed a portion had been or would be paid by the corporation to the proper officer for the receipt of taxes. The certificate further indicated that the dividend payment was equivalent to a gross dividend less income tax "appropriate thereto" at the current rate in the case of a dividend "free of tax," or that the warrant represented the net amount of a gross dividend less income tax "appropriate thereto" at the current rate in the case of a dividend "less tax."

The question is whether the amounts shown on the certificates accompanying dividend payments as taxes "appropriate to" such dividends may be taken as a credit against the Federal income tax as income taxes paid or accrued to a foreign country within the meaning of Section 131 (a) of the Reve-

nue Act of 1928, subject to the limitation imposed by Section 131 (b), and whether any balance not available as a credit may be deducted from gross income under Section 23 (c) of that Act.[1]

STATUTE INVOLVED

The pertinent portions of the statute involved are printed in the Appendix, *infra*, pp. 19–21.

STATEMENT

Throughout the year 1929 the taxpayer, Mary Duke Biddle, a citizen of the United States, owned certain ordinary shares of capital stock in British-American Tobacco Company, Limited, and certain shares of ordinary and deferred stock in Tobacco Securities Trust Company, Limited. These companies are corporations organized and existing under the laws of Great Britain with their head offices in England. (R. 25–26.)

During the calendar year 1929 these corporations declared and paid cash dividends upon their outstanding stock of the classes noted above. The rates of such dividends and dates of payment are given in detail in the record, pp. 26–29. The dividends on British-American Tobacco Company

[1] A cognate question is whether the amounts shown as taxes "appropriate to" such dividends should be added to the net amount actually received as dividends in determining the amount of gross income. If they should be held to be taxes paid by the respondent, they obviously should be included in his gross income.

stock were paid "free of British Income Tax," and the dividends on stock in Tobacco Securities Trust Company were paid "less British Income Tax" (R. 26, 28, 32–40). By communications transmitted to their shareholders at the time the dividend warrants were transmitted the above companies certified to their shareholders that British income taxes and Dominion income taxes on the profits of the company of which the dividends formed a part had been paid or would be paid by the company to the proper officer for the receipt of taxes (R. 27–29, 32–40). The certificates transmitted to its shareholders by British-American Tobacco Company indicated that the dividend paid was equivalent to a gross dividend of a stated amount less the amount of income tax "appropriate to" the gross dividend (R. 27, 32–37). The certificates transmitted to its shareholders by the Tobacco Securities Trust Company indicated a gross dividend of a stated amount, less income tax "appropriate to" such gross dividend, and the net amount of the dividend for which the voucher was issued (R. 28, 38–41).

The net amounts received during the year by the taxpayer as dividends on such shares of stock, stated in terms of United States money, the amounts certified as British and Dominion income taxes "appropriate thereto," and the aggregate of these amounts, treated as gross dividends, were as follows (R. 27–30):

Corporation	Net dividend received	Amount shown as tax "appropriate thereto"	Amount shown as gross dividend
British-American Tobacco Co., Ltd.	[1] $180,196.86	$45,049.22	$225,246.08
Tobacco Securities Trust Co., Ltd.	13,209.25	2,331.05	15,540.30
Total	193,406.11	47,380.27	240,786.38

[1] These figures are computed at the rate of exchange prevailing at the time of each distribution.

It is the amount shown above as taxes "appropriate to" the dividends received by the taxpayer which gives rise to the present controversy.

In her income tax return for 1929 the taxpayer included in gross income, as dividends received from foreign corporations, the sum of $241,757.64 (R. 45–50). It was stipulated before the Board of Tax Appeals that if her method of reporting income is correct the amount to be included in gross income as dividends from foreign corporations is $240,786.38, which is the total amount of cash received as dividends plus the amounts certified as British income taxes "appropriate thereto" (R. 30). The taxpayer claimed the amounts certified as British income taxes "appropriate to" her dividends as a credit under Section 131 (a) of the Revenue Act of 1928 against her Federal income tax, subject to the limitations imposed upon such credit by Section 131 (b), and the balance not allowable as a credit was claimed as a deduction from income under Section 23 (c) of the Act. These provisions are printed in the Appendix, *infra*, pp. 19–21. The amount actually claimed as a

credit under Section 131 (a), *supra,* was $36,458.04, and the amount of $11,893.49 was deducted from gross income under Section 23 (c) of the Act (R. 30–31, 45–50, 53–55). The correct amount of taxes "appropriate to" the dividends, however, was stipulated to be $47,380.27 (R. 30).

The taxpayer kept her books of account and made her income tax returns upon the basis of cash receipts and disbursements (R. 31, 107).

In auditing the taxpayer's return for 1929 the Commissioner made several adjustments to income which resulted in the determination of a substantial deficiency in tax (R. 9–17). In making his determination, however, he made no change in the amount of $241,757.64 reported as dividend income from foreign corporations (R. 11, 15). Of the amount of $48,351.53 treated as British income taxes "appropriate to" the dividends, the Commissioner allowed $36,232.57 as a credit against Federal income taxes and allowed the balance of $12,118.96 as a deduction from gross income (R. 15, 31).

The taxpayer appealed to the Board of Tax Appeals, alleging error with respect to the several adjustments made by the Commissioner in his deficiency notice (R. 6–9). By amended answer the Commissioner affirmatively alleged error on his part in allowing any credit or deduction of the amounts certified as British income taxes "appropriate to" the dividends received from British-American Tobacco Company and Tobacco Securi-

ties Trust Company (R. 20–22). All issues raised by the taxpayer's petition were settled by stipulation, reserving for decision by the Board only the issues raised by the Commissioner's amended answer (R. 24–25). The Board of Tax Appeals, in an opinion disposing of this and four other appeals, including an appeal by George W. Elkins, involving the same questions, held that only the net amount of cash received by the taxpayer as dividends from the above foreign corporations should be included in gross income, and that no credit or deduction should be allowed on account of the amounts certified as British income tax "appropriate to" such dividends (R. 104–119).

Appeals from the decision of the Board of Tax Appeals were taken to the Circuit Court of Appeals for the Third Circuit by George W. Elkins, and to the Circuit Court of Appeals for the Second Circuit by this taxpayer. The Board's decision was affirmed in the instant case by the Circuit Court of Appeals for the Second Circuit (R. 585), but was reversed by the Circuit Court of Appeals for the Third Circuit in the *Elkins* case. *Elkins* v. *Commissioner,* 91 F. (2d) 534. Certiorari has been granted in both cases to resolve this conflict. The *Elkins* case is No. 505, present Term.

SUMMARY OF ARGUMENT

The question presented here arises on a similar record in *Helvering* v. *Elkins,* No. 505, present Term; and the argument to be presented here is

fully developed in the brief for the petitioner in that case. Accordingly, that brief is incorporated herein by reference.

The petitioner contends that this case involves a pure question of fact—whether the taxpayer is "regarded" under British law as having paid a tax—and that the Board's finding that she is so regarded is conclusive. We believe that while foreign law is a question of fact, its construction and effect is a question of law for the courts to decide.

If, under British law, the taxpayer can be said to be regarded as a taxpayer, it is only, we submit, for the specific purpose of administering relief provisions and computing the surtax. This, even if true, does not determine the question here—whether the petitioner paid such a tax to a foreign government as is contemplated by our Revenue Acts. We believe that under British law the petitioner has not paid an exaction to the British Government in the form of a tax.

ARGUMENT

NO TAX AT THE STANDARD RATE IS IMPOSED BY GREAT BRITAIN UPON THE PAYMENT OR RECEIPT OF DIVIDENDS. PETITIONER PAID NO SUCH TAX AND IS NOT ENTITLED TO THE CLAIMED CREDIT

This case presents the same question as *Helvering* v. *Elkins,* No. 505, present Term, with which it was tried before the Board of Tax Appeals. There are no essential variations between the records of the two cases except as to names and

amounts. The arguments of the Government on the questions presented in both the cases are fully developed in the Brief for the Petitioner in the *Elkins* case, p. 11 *et seq.,* and that brief is incorporated herein by reference. This Court is respectfully referred thereto. However, in so far as it is deemed that the arguments of the petitioner need particular reply, we present the following argument.

Section 131 (a) of the Revenue Act of 1928, *infra,* p. 20, permits taxpayers to deduct "income, war-profits, and excess-profits taxes paid or accrued during the taxable year to any foreign country * * *." Since only those credits and deductions specifically authorized by statute are allowable, the burden is upon the petitioner to show that the amounts involved were income, war-profits or excess profits taxes within the meaning of the statute, that they were paid during the taxable year, and that they were paid to a foreign government.

Under authority of Section 131 (a), *supra,* petitioner claims the right to deduct amounts designated as "taxes appropriate" to certain dividends, on the ground that these sums represented taxes deducted and withheld from dividends by the British corporations. In support of her contention petitioner has introduced official copies of the Acts of Parliament, decisions of the British courts, and the testimony of Talbot, an English barrister, who was qualified as an expert on English tax law. Upon

this evidence the Board of Tax Appeals found that stockholders of English corporations receiving dividends are regarded by the British income-tax Acts as having paid, by deduction or otherwise, the tax appropriate to the dividend; that the amount appropriate to the dividend is required to be included in the taxpayer's gross income for the sole purpose of computing the surtax upon large incomes,[2] and that a stockholder of small income is entitled, within the provisions of the British income tax Acts, to claim a refund by way of relief of the tax appropriate to the dividend (R. 110–111). The Board held, however, that the British income tax Acts impose no tax upon the payment of a dividend; that the stockholder receiving a dividend has no liability for tax at the standard rate with respect to the dividend received by him; that the British corporation in paying its own income tax does not pay a tax for its stockholders nor discharge any obligation resting upon the stockholders; and that petitioner is not entitled to the claimed credit (113, 115, 118).

Petitioner contends that the case involves a pure question of fact, and that the Board's finding that the stockholder is "regarded" in England as having paid a tax should have precluded the Board and the court below from holding otherwise than for the taxpayer, and is, furthermore, conclusive

[2] Only the tax at the standard rate is involved. It has been conceded that the English stockholder is entitled to credit in so far as he pays a surtax.

upon this Court. We submit that the laws of England are material only in so far as they disclose whether an exaction in the form of a tax is imposed by the British Government upon stockholders receiving dividends, and, if so, whether such liability is satisfied and discharged by payments to the British Crown of the sums appropriate to the dividends.

While foreign law is a question of fact, to be proven as any other fact, the construction and effect of the foreign law is a question of law for the court to decide. *Bank of China* v. *Morse,* 168 N. Y. 458, 469–470; *Hanna* v. *Lichtenhein,* 225 N. Y. 579, 582–583; *Minero* v. *Ross and Masterson,* 106 Tex. 522, 535–536. In *Hanna v. Lichtenhein, supra,* the court said (pp. 582–583):

> Foreign law is a question of fact and must be proved as such, but when after such proof is given the questions involved depend upon the construction and effect of a statute or judicial opinion they are for the court and not questions of fact at all.

This is clearly the true rule, supported by the great weight of authority. *Fitzpatrick* v. *International Ry. Co.,* 252 N. Y. 127, 136–137, annotated, 68 A. L. R. 809. While there appears to be some divergence of view in the state courts, the rule stated is clearly the law in the Federal courts. *Eastern Building &c. Assn.* v. *Williamson,* 189 U. S. 122, 126–127; *Finney* v. *Guy,* 189 U. S. 335, 342; *Scheer*

v. *Rockne Motors Corp.*, 68 F. (2d) 942, 945 (C. C. A. 2d).

Here, decisions of the British courts were introduced in evidence, and hence it was the duty of the court to determine for itself what those decisions held. However, if it can be said that the British law regards the shareholder as a taxpayer, rather than the person who bore the ultimate burden of the corporation's income tax liability, it is only for the purpose of administering the relief provisions already referred to and for the purpose of requiring the inclusion in gross income, for purposes of the surtax, of the amount of net dividend received plus income tax "appropriate thereto." But the fact that British law requires the inclusion of this amount in gross income, or that it takes this amount into consideration in administering its relief provisions is not determinative of the question involved here. This Court pointed out in *Merchants L. & T. Co.* v. *Smietanka*, 255 U. S. 509, 521–522, that the British taxing Acts are quite different from our Acts.

The British concept of income differs from ours and any inferences drawn from the fact that under British law an item is treated as income would be misleading in the determination of the status of the same item as income under our law. As pointed out by the Circuit Court of Appeals for the Second Circuit in *F. W. Woolworth Co.* v. *United States*, 91 F. (2d) 973, now pending before this Court on petition for a writ of certiorari, No. 568,

present Term, the British shareholder must compute his super tax upon a nominal dividend which he never receives. Such a practice finds no counterpart in our law and it is futile to attempt to rationalize it with our tax system and constitutional limitations.

The English decisions and the testimony of the British expert clearly show that the amount certified as "taxes appropriate" to a dividend is not paid to the Crown; that the so-called deduction is merely a device which serves the purpose of enabling the British Government to charge the stockholder for surtax purposes with the receipt of the gross dividend and which forms the basis for refunds to taxpayers who are wholly or in part exempt. Thus the British taxpayer liable to surtax pays a tax on dividends he never received, and the exempt taxpayer receives a refund for a tax he never paid. *F. W. Woolworth Co.* v. *United States, supra,* p. 975. This is the basis upon which the taxpayer is regarded in England as a taxpayer. However, it is clear that "taxpayer" is only a term of convenience and that no liability to the Government is imposed upon the stockholder receiving a dividend, and that nothing is withheld by the corporation and paid to the British Government on his behalf.

The British practice will be more readily understood when it is appreciated that a British corporation is permitted to declare dividends in the amount of its entire profits without reduction on

account of the income tax it has paid or will pay on its own account upon those profits. Thus a British corporation having a profit of £1,000 and paying an income tax thereon of £250 declares a gross dividend of £1,000. Since the corporation in fact has only £750 to distribute, it is apparent that the amount of the dividend is a fiction (R. 147–148). The process of harmonizing the amount of the dividend declared with the actual profits distributed is to reduce the gross dividend by £250, and to designate this latter amount as the "tax appropriate to the dividend." It is clear that this involves no deduction and no withholding. An American corporation would simply declare a dividend in the amount of its total profits and the American stockholders obviously would not suffer any withholding or any deduction, because they would actually receive all the corporate profits available for dividends.

Thus this case arises because of the practice allowed under British law of declaring dividends greater in amount than the profits and the reduction of the declared amount to that which is actually distributed. This does not involve paying a tax, either by the shareholder or by the corporation on his behalf. It does not involve an actual reduction of the dividend or the withholding of any amount by the corporation. It does not involve even an actual recoupment by the corporation or the actual passing on of the tax, although the British authorities explain it as such. The

only tax actually paid is that imposed upon the profits the corporation has made, which is paid by the corporation and which bears no necessary relation to the amount "appropriate to" the dividend (R. 185–187). The important factor of the British practice is the fiction of regarding all corporate profits as available for dividends despite the fact that a portion has been or will be used to pay the corporate tax. We submit that such a practice does not support petitioner's claim that she has paid an exaction to the British Government in the form of a tax.

Petitioner cites (Br. 13–14) an excerpt from the opinion in *Elkins* v. *Commissioner,* 91 F. (2d) 534, 538 (C. C. A. 3d), now pending on a writ of certiorari, No. 505, present Term, wherein *Old Colony Tr. Co.* v. *Commissioner,* 279 U. S. 716, is relied upon for the suggestion that the Federal Revenue Acts recognize the constructive payment of taxes. In the *Old Colony Tr. Co.* case, however, there was an actual payment of taxes to the United States Government by the taxpayer's employer for and on behalf of the taxpayer. We believe that the payment there was an indirect payment and not a constructive payment. But in any event it is clear that the *Old Colony Tr. Co.* case presents a payment which differs from what is termed a constructive payment of the English tax. The difference lies in the fact that the British Government imposes no exaction of any kind upon the payment or receipt of a dividend and receives nothing directly

or indirectly for or on behalf of either the corporation paying the dividend or the stockholder receiving it. A British corporation pays an income tax upon its profits and that tax is neither increased nor diminished when the corporation thereafter pays a dividend to its stockholders. In other words, the payment of a dividend does not increase the tax receipts of the British Crown, except, of course, to the extent that a surtax is incurred by the stockholders. There is no question of the surtax involved here.

Petitioner's contention that the English tax appropriate to the dividends finds its counterpart in our deduction of taxes at the source overlooks the fact that our taxes actually produce revenue, while the purported English equivalent results in no enrichment of the Crown. The British corporation paying a dividend is not required to withhold any amount, and if it does deduct a tax appropriate to the dividend, it does not turn the amount of the deduction over to the British Treasury. Instead, it keeps it. The process is variously described as "withholding," "deducting," "reimbursing itself," and "passing the tax on." These are not, in our tax law, synonymous terms, and the variety of the terminology is indicative of the artificiality of the entire British practice to our system of taxation.

We do not contend that there is no instance in the English tax collection system of the deduction of taxes at the source. Apparently there are in-

stances where the person deducting pays the amount deducted over to the Crown. The frequency of reference to such a practice indicates as much. But it is clearly shown here that when the term "deduction at the source" is applied to dividends its reference is only to the device whereby a declared dividend in excess of the corporation's ability or willingness to pay is reduced to the amount available for a dividend.

The statements made in *Brooke* v. *Commissioners of Inland Revenue,* 7 British Tax Cases 236 (R. 217, 233, 245), and *Hamilton* v. *Commissioners of Inland Revenue,* 16 British Tax Cases 213 (R. 366, 405), relied on by petitioner (Br. 24–25) must be weighed against the indubitable facts: (1) that the corporation paying a dividend is not *required* to make any "deduction," but is merely *permitted* to do so; and thus there is no imposition of a tax by the sovereign; (2) that the deduction is merely a device to reduce an excessive declaration of dividends (R. 147); and (3) that the amount which is treated as a "deduction" is not paid over to the British Government (R. 164–165, 171, 181, 189, 199). These cases must also be read in the light of the fact that in a later case, *Neumann* v. *Commissioners of Inland Revenue,* 18 British Tax Cases 332, it was held in the House of Lords that there is, strictly speaking, no tax on dividends at all (R. 424, 472, 479).

CONCLUSION

In view of the foregoing, we respectfully submit that the decision below should be affirmed.

STANLEY REED,
Solicitor General.
JAMES W. MORRIS,
Assistant Attorney General.
SEWALL KEY,
J. LOUIS MONARCH,
F. E. YOUNGMAN,
Special Assistants to the Attorney General.
STEPHEN M. FARRAND,
Attorney.

DECEMBER 1937.

APPENDIX

Revenue Act of 1928, c. 852, 45 Stat. 791:

SEC. 22. GROSS INCOME.

(a) *General definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever.

* * * * *

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * *

(c) *Taxes generally.*—Taxes paid or accrued within the taxable year, except—

(1) income, war-profits, and excess-profits taxes imposed by the authority of the United States;

(2) so much of the income, war-profits, and excess-profits taxes imposed by the authority of any foreign country or possession of the United States as is allowed as a credit against the tax under section 131; and

(3) taxes assessed against local benefits of a kind tending to increase the value of the property assessed; but this paragraph shall not exclude the allowance as a deduc-

tion of so much of such taxes as is properly allocable to maintenance or interest charges.

For the purpose of this subsection, estate, inheritance, legacy, and succession taxes accrue on the due date thereof, except as otherwise provided by the law of the jurisdiction imposing such taxes, and shall be allowed as a deduction only to the estate.

* * * * *

SEC. 115. DISTRIBUTIONS BY CORPORATIONS.

(a) *Definition of dividend.*—The term "dividend" when used in this title (except in section 203 (a) (4) and section 208 (c) (1), relating to insurance companies) means any distribution made by a corporation to its shareholders, whether in money or in other property, out of its earnings or profits accumulated after February 28, 1913.

* * * * *

SEC. 131. TAXES OF FOREIGN COUNTRIES AND POSSESSIONS OF UNITED STATES.

(a) *Allowance of credit.*—The tax imposed by this title shall be credited with:

(1) *Citizen and domestic corporation.*—In the case of a citizen of the United States and of a domestic corporation, the amount of any income, war-profits, and excess-profits taxes paid or accrued during the taxable year to any foreign country or to any possession of the United States; and

(2) *Resident of United States.*—In the case of a resident of the United States, the amount of any such taxes paid or accrued during the taxable year to any possession of the United States; and

(3) *Alien resident of United States.*—In the case of an alien resident of the United States, the amount of any such taxes paid or accrued during the taxable year to any foreign country, if the foreign country of which

such alien resident is a citizen or subject, in imposing such taxes, allows a similar credit to citizens of the United States residing in such country; and

(4) *Partnerships and estates.*—In the case of any such individual who is a member of a partnership or a beneficiary of an estate or trust, his proportionate share of such taxes of the partnership or the estate or trust paid or accrued during the taxable year to a foreign country or to any possession of the United States, as the case may be.

(b) *Limit on credit.*—In no case shall the amount of credit taken under this section exceed the same proportion of the tax (computed on the basis of the taxpayer's net income without the deduction of any income, war-profits, or excess-profits tax any part of which may be allowed to him as a credit by this section), against which such credit is taken, which the taxpayer's net income (computed without the deduction of any such income, war-profits, or excess-profits tax) from sources without the United States bears to his entire net income (computed without such deduction) for the same taxable year.

* * * * *

(e) *Proof of credits.*—These credits shall be allowed only if the taxpayer furnishes evidence satisfactory to the Commissioner showing the amount of income derived from sources without the United States, and all other information necessary for the verification and computation of such credits.

U. S. GOVERNMENT PRINTING OFFICE: 1937